

**REPORT OF THE AUDITOR-GENERAL TO THE NORTHERN CAPE PROVINCIAL
LEGISLATURE AND THE COUNCIL ON PHOKWANE LOCAL MUNICIPALITY**

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the financial statements of the Phokwane Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2012, the statements of financial performance, changes in net assets and cash flows for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting Officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards on Generally Recognised Accounting Practice (SA Standards of GRAP), the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Revenue

4. I was unable to obtain sufficient appropriate audit evidence regarding government grants and subsidies, fines revenue, service charges, licenses and permits, income from agency fees and other income in the statement of financial performance to the amount of R166 566 671 (2011: R175 591 315).
 - (a) The accounting policy of the municipality states that fine revenue constitutes both spot fines and summonses. The listings of these items that should have been included in fine revenue were not submitted for audit purposes.
 - (b) Registers and monthly reconciliations were not implemented to ensure that all other income is included in the financial statements.
 - (c) Certain water meters and electricity meters were identified that did not reflect on the meter reading listing and consumption was consequently not levied.
 - (d) External confirmation for government grants and subsidies amounting to R5 138 433 was not submitted. In addition documentation was not submitted to confirm that an amount of R466 162 should have been included as grant revenue.
 - (e) Prior year reconciliations were not performed for prepaid electricity that was sold on behalf of the municipality to the amount of R12 244 530.

- (f) Documentation to confirm that service charges and fines revenue was included in the correct period was not submitted for audit purposes.
- (g) A contract to confirm the amounts that should have been received from an external party to confirm the journals processed for agency fees to the amount of R408 422 were not submitted.
- (h) As described in note 32 to the financial statements, the restatement of R14 197 298 was made in order to rectify a prior year misstatement. I was unable to confirm the restatement by alternative means.
- (i) Prior year documentation confirming the processing of journals of R136 509 154 processed against revenue items could not be obtained. These transactions were passed against refuse removal, sewerage and sanitation charges, government grants and subsidies and rental of facilities and equipment.
- (j) During 2011 I was unable to audit the difference between the trial balance and the amounts disclosed in the annual financial statement to the amount of R3 445 592.

Alternative procedures could either not be performed or were not successful. Consequently I was unable to determine whether any adjustment relating to revenue in the financial statements was necessary.

- 5. The financial statements did not include the agency fee portion accrued to the municipality of revenue received on behalf of third parties for licences and permits as required by Standards of Generally Recognised Accounting Practice, GRAP 9, Revenue from exchange transactions. I was unable to determine the correct value of agency fees, operating expenditure and cash and cash equivalents to be separately disclosed as it was impracticable to do so.
- 6. Internal controls were not implemented as required by Standards of Generally Recognised Accounting Practice, GRAP 9, Revenue from exchange transactions, to ensure that all consumers were billed for consumption of service charges. Consumption of services were not always charged to consumers, were not always charged at the correct rates and were at times charged on estimated amounts for a number of months. I was unable to determine the correct value of service revenue and receivables from exchange transactions to be separately disclosed as it was impracticable to do so.
- 7. The incorrect valuation roll was used in the prior year. Property rates and trade and other receivables were overstated by R1 609 349. Rebates were not applied to all consumer accounts that lead to the understatement of rebates and receivables are overstated by R1 207 227 in contravention with Standards of Generally Recognised Accounting Practice, GRAP 23, Revenue from non-exchange transactions.
- 8. The incorrect tariffs were used during the prior year in contravention of Standards of Generally Recognised Accounting Practice, GRAP 9, Revenue from exchange transactions. Service charges for water were understated and trade receivables from exchange transactions overstated by R786 182.

Property, plant and equipment

- 9. I was unable to obtain sufficient appropriate audit evidence regarding property plant and equipment to the amount of R184 628 535 (2011: R170 056 638) due the following

matters:

- (a) Infrastructure assets and other assets stated at R12 770 839 in the financial statements were not presented for physical verification. Certain infrastructure assets were identified which could not be traced to the fixed asset register. Movable assets identified during physical verification could not be located on the fixed asset register.
 - (b) External documentation for the assumptions used to value infrastructure assets was not available.
 - (c) The contract with a water supplier was not submitted. It was not possible to determine whether the assets purchased through the agreement were the assets of the municipality or those of the third party.
 - (d) A condition assessment was not always made for all assets. In the instances where a condition assessment was made regarding assets classified as scrap, these assets were not fully depreciated.
 - (e) Not all assets were unbundled into separately depreciable parts.
 - (f) Assets in the name of the municipality identified through deed searches could not be traced to the general ledger.
 - (g) The opening balance of accumulated depreciation exceeds the accumulated depreciation per the trial balance for other assets by an amount of R277 863. The opening balance of accumulated depreciation per the general ledger exceeds the amount per the fixed asset register by R372 488. The cost price and accumulated depreciation of assets included in the financial statements exceeds the amount per the general ledger by R4 811 104. The depreciation for per the disclosure note exceeds the amount per the trial balance by R346 812.
 - (h) Properties that are rented to employees at below market-rated rentals were not included in the financial statements.
 - (i) Supporting documentation for the restatement of R1 568 769 that was made in order to rectify a prior year misstatement was not submitted for audit purposes.
10. The municipality did not depreciate property, plant and equipment, as required by Standards of Generally Recognised Accounting Practice, GRAP 17 Property, plant and equipment. The error occurred due to an incorrect calculation of prior year depreciation. The effects on the financial statements are that property, plant and equipment, net profit and accumulated profits are understated by R38 109 437.

I was unable to confirm these matters by alternative means. Consequently, I was unable to determine whether any adjustment relating to movable tangible assets in the financial statements was necessary.

Cash and cash equivalents

11. During 2011 I was unable to obtain sufficient appropriate audit evidence for journal entries amounting to R49 643 976, and unreconciled bank reconciliations as disclosed in note 19 to the financial statements to the amount of R10 541 706. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustments to the cash and cash equivalents corresponding figure was necessary. My audit opinion on the financial statements for the period ended 30 November 2012 was modified accordingly. My opinion on the current period's financial statements is also

modified because of the possible effect of this matter on the comparability of the current period's figures.

Receivables from exchange and non-exchange transactions

12. I was unable to obtain sufficient appropriate audit evidence regarding receivables from exchange and non-exchange transactions to the amount of R14 893 863 (2011: R12 877 421) for the following matters:
- (a) Payments, external confirmation and any other documentation confirming receivables amounting to R38 351 792 were not submitted for audit purposes.
 - (b) The receivable age analysis and the financial statements at 30 June 2011 did not agree as a difference of R2 557 566 was identified. The accuracy of the impairment of trade receivables amounting to R81 406 411 could therefore not be verified due to this material difference between the receivable age analysis and the financial statements.
 - (c) A listing and supporting documentation for other consumer arrears disclosed as R30 953 573 in the prior year were not submitted for audit purposes.
 - (d) Supporting documentation for credit balances to the amount of R3 151 484 (2011: R2 846 476) and journal entries passed in the prior year was not submitted.
 - (e) Detailed listings and support to confirm the restatement of R982 944 that was made in order to rectify a prior year misstatement were not submitted for audit purposes.

Alternative procedures could not be performed. Consequently, I was unable to determine whether any adjustment relating to receivables from exchange and non-exchange transactions in the financial statements was necessary.

13. The recoverability of debtors was not evaluated for impairment per financial asset or group of financial assets as required by Standards of Generally Recognised Accounting Practice, GRAP 104, Financial instruments. I was unable to determine the correct value of receivables from exchange and non-exchange transactions and the corresponding adjustment to the provision for doubtful debt to be separately disclosed as it was impracticable to do so.
14. Trade receivables and revenue were understated by R3 528 270 in the prior year, as interest was charged on the outstanding debtor accounts for services by using the incorrect tariff contrary to Standards of Generally Recognised Accounting Practice, GRAP 104, Financial instruments.

Employee cost

15. I was unable to obtain sufficient appropriate audit evidence regarding employee cost to the amount of R32 035 733 (2011: R32 099 969) for the following matters:
- (a) Employment contracts, appointment letters, timesheets, clock cards or attendance registers regarding salaries and wages, allowances and housing benefits were not submitted for salaries and wages amounting to R13 822 149 (2011: R2 712 088)

- (b) A difference to the amount of R290 854 was identified between the amount that should have been paid to the councilors and the amount that was paid according to the general ledger.
 - (c) Documentation to confirm prior year journal entries of R143 523 passed against employee-related cost was not submitted for audit purposes.
 - (d) A prior year difference of R297 284 between the payroll and the financial statement could not be explained with supporting documentation.
16. Allowances were paid in excess of the collective agreements contrary to the requirements of SA Standards of GRAP 1, Presentation of financial statements. Employee cost is overstated and receivables are understated by R534 174 respectively.

Alternative procedures could not be performed. Consequently, I was unable to determine whether any adjustment relating to employee cost in the financial statements was necessary.

Operating expenditure

17. I was unable to obtain sufficient appropriate audit evidence regarding operating expenditure to the amount of R30 487 773 (2011: R80 182 438) for the following matters:
- (a) A listing of the reconciling item disclosed as assets uncleared in the expenditure note amounting to R934 234 was not submitted for audit purposes.
 - (b) Documentation supporting prior year journal entries amounting to R3 497 158 passed against expenditure items was not submitted. These transactions were passed against grants and subsidies paid, finance charges, general expenditure, repairs and maintenance and bulk purchases.
 - (c) Indigent application forms were not submitted to confirm that the indigent subsidies were correctly calculated and included as an expenditure item grants and subsidies paid.
 - (d) As described in note 32 to the financial statements, the restatement of R13 100 724 was made in order to rectify a prior year misstatement. I was unable to confirm the restatement by alternative means.

Alternative procedures could not be performed. Consequently, I was unable to determine whether any further adjustment relating to operating expenditure in the financial statements was necessary.

18. During 2011 finance charges and long-term liabilities were understated by R160 379 as not all interest paid was disclosed as required by Standards of Generally Recognised Accounting Practice, GRAP 1, Presentation of financial statements.

Accumulated surplus

19. I was unable to obtain sufficient appropriate audit evidence for the balance of accumulated surplus disclosed as R218 839 704 (2011: R188 550 727) in the statement of changes in net assets due to the following:
- (a) Corrections of errors were processed to revenue and expenditure of the prior year to the amount of R546 572 (2011: R13 531 548) for which listings of the errors and documentation thereof were not submitted for audit purposes.
 - (b) During 2011 an unexplained difference of R9 409 487 existed between the financial statements and the trial balance.

Alternative procedures could not be performed. Consequently, I was unable to determine whether any adjustment relating to accumulated surplus in the financial statements was necessary.

20. The nature of the corrections of errors as disclosed in note 32 to the financial statements were not always disclosed as required by Standards of Generally Recognised Accounting Practice, GRAP 3, Accounting policies and changes in accounting estimates.

Unpaid conditional grants

21. I was unable to obtain sufficient appropriate audit evidence for the balance of unpaid conditional grants disclosed as R4 917 738 (2011: R7 797 087) in note 9 to the financial statements due to the limitations communicated in paragraphs xx of this report. Alternative procedures could not be performed. Consequently, I was unable to determine whether any further adjustment relating to unpaid conditional grants in the financial statements was necessary.
22. The unpaid conditional grant opening balance of R4 128 210 for the Municipal Infrastructure Grant which constitutes a current asset was incorrectly off-set in terms of paragraph 39 of SA Standards of GRAP 1 Presentation of financial statements, against the unspent portion of R2 879 349. Unspent conditional grants and unpaid conditional grants are understated by R2 879 349 respectively.
23. Unspent conditional grants, unauthorised and general expenditure of the prior year were understated by R5 967 139 in respect of over-expenditure on projects relating to the municipal infrastructure grant of R4 128 210, integrated national electrification grant of R1 044 260 and other grants of R794 669 disclosed in note 21 to the financial statements. This was contrary to the requirements of SA Standards of GRAP 23, Revenue from non-exchange transactions. Furthermore revenue for grants was disclosed as R98 400 183 in the statement of financial performance. The amount for which the grant conditions were met that should have been disclosed as revenue amounted to R69 397 302. This resulted in revenue and capital expenditure being overstated by R29 002 881. Included in this overstatement were funds that were received from the Department of Cooperative Governance, Human Settlements and Traditional Affairs for which the municipality acts as an implementing agent.

Irregular expenditure

24. I was unable to obtain sufficient appropriate audit evidence for irregular expenditure disclosed as R8 651 655 (2011: R5 171 537) in note 39 to the financial statements due to the following matters:
 - (a) An unexplained difference exists between the irregular expenditure listing and the financial statements to the amount of R585 527.
 - (b) Included in the irregular expenditure disclosed in note 39 is an amount of R5 171 537 that relates to prior year irregular expenditure. A detailed listing of the items that consist of the amount was not submitted for audit purposes.
 - (c) In addition, I could not obtain reasonable assurance on the completeness of irregular expenditure as the auditee does not have an adequate system in place that will detect and record irregular expenditure incurred.

Alternative procedures could not be performed. Consequently, I was unable to determine whether any adjustment relating to irregular expenditure in the financial statements was necessary.

25. The irregular expenditure disclosed as R8 651 655 (2011: R5 171 537) in note 39 to the financial statements was understated due to instances of non-compliance with laws and regulations not being identified and disclosed by the municipality. I was unable to determine the correct value of commitments to be separately disclosed as it was impracticable to do so.

Taxes

26. I was unable to obtain sufficient appropriate audit evidence regarding taxes to the amount of R10 993 425 (2011: R12 407 416) for the following matters.
- (a) A difference to the amount of R785 806 between the general ledger and the recalculation of value-added tax (VAT) that could have been claimed from the South African Revenue services.
 - (b) A difference between the VAT control account and the VAT 201 return submitted for August 2011 (June 2011) to the amount of R498 514 (2011: R870 630) was identified.
 - (c) Sufficient appropriate audit evidence could not be obtained for prior year transactions processed against the VAT control account of R102 849 150.

Alternative procedures could not be performed. Consequently, I was unable to determine whether any further adjustment to the taxes figure was necessary.

27. VAT is understated and expenditure is overstated by R1 017 798 (2011: R1 987 514) as VAT was claimed on invoices that did not meet the definition of valid tax invoices as per section 20 (4) of the Value-Added Tax Act No. 89 of 1991) (VAT Act).
28. Internal controls are not in place to declare output VAT on debtors with credit balances that had not been refunded to consumers within four months as required by section 8(27) of the VAT Act. I was unable to determine the correct value of VAT and trade and other payables to be separately disclosed as it was impracticable to do so.
29. The total amount of contributions to organised local government for the financial year and the prior year, and the amount of any contributions outstanding as at the end of the financial year regarding VAT are understated. Disclosures were not made for VAT in note 40.3 to the financial statements, as required by section 125(1) (b) of the MFMA. I was unable to determine the correct value of VAT to be separately disclosed as it was impracticable to do so.

Trade and other payables

30. I was unable to confirm trade and other payables stated at R5 896 885 (2011: R11 886 998) in note 8 to the financial statements due the following matters.
- (a) A detailed listing of items included in suspense accounts to the amount of R491 926 (2011: R492 015) was not submitted for audit purposes.
 - (b) A detailed listing and documentation to confirm the restatement of R13 766 542 that was made in order to rectify a prior year misstatement were not submitted for audit purposes.

I was unable to perform alternative procedures. Consequently, I was unable to determine whether any adjustment relating to trade and other payables in the financial statements was necessary.

31. Current year expenditure that was paid after year end was not included in the financial statements as required by Standards of Generally Recognised Accounting Practice, GRAP 1, Presentation of financial statements. I was unable to determine the correct value of expenditure and payables to be separately disclosed as it was impracticable to do so.

Employee benefits

32. I was unable to obtain sufficient appropriate audit evidence regarding employee benefits to the amount of R15 545 888 (2011: R2 392 720) for the following matters:
- (a) The municipality did not have adequate systems in place during the prior year to maintain records of leave, which resulted in leave being understated by R957 088. In addition, sufficient appropriate audit evidence was not available for the prior year amounts disclosed as leave in note 6 to the financial statements.
 - (b) The relevant documents supporting the assumptions used to calculate the employee benefits in the financial statements were not always submitted for audit purposes.

Alternative procedures could not be performed. Consequently, I was unable to determine whether any adjustment relating to employee benefits in the financial statements was necessary.

Investment property

33. I was unable to obtain sufficient appropriate audit evidence regarding investment property to the amount of R3 536 463 (2011: R3 536 463) for the following matters disclosed in note 12 to the financial statements:
- (a) Properties to the amount of R543 950 were not available for physical verification due to the location of these assets not being available.
 - (b) Property included as vacant land was identified that was not vacant during physical verification. The lease agreements of these properties to the amount of R597 608 were not submitted for audit purposes.
 - (c) Buildings that are leased from the municipality were not included in investment property. Lease agreements were not submitted for audit purposes.

I was unable to confirm the matters by alternative means. Consequently, I was unable to determine whether any further adjustment to the investment property figure was necessary.

Inventory

34. The municipality did not have adequate systems in place to identify and disclose water inventory in the annual financial statements, as required by Standards of Generally Recognised Accounting Practice, GRAP 12, Inventory. I was unable to determine the correct amount of water inventory as it was impracticable to do so.
35. Municipal erven that were used to build social housing and that had not yet been transferred at year end were not included as inventory as per Standards of Generally Recognised Accounting Practice, GRAP 12, *Inventory*. Inventory and accumulated surplus are understated and investment property is overstated in the current and prior year. I was unable to determine the correct value of inventory to be separately disclosed in the current

year as it was impracticable to do so.

36. Inventory is understated and investment property is overstated by R4 620 955 in the prior year in respect of land intended to be sold which was not disclosed per Standards of Generally Recognised Accounting Practice, GRAP 12, Inventory. The municipality did not disclose municipal land available for sale. I was unable to determine the correct value of inventory to be separately disclosed in the current year as it was impracticable to do so.

Provisions

37. I was unable to confirm the provision for landfill sites stated at R4 429 126 (2011: R4 218 215) in note 4 and 7 to the financial statements due to the detailed assumptions and supporting documentation used by the expert to value the landfill sites not being submitted. I was unable to perform alternative procedures. Consequently, I was unable to determine whether any adjustment relating to provisions in the financial statements was necessary.
38. All landfill sites and refuse dumping sites that should be provided for future rehabilitation as required by Standards of Generally Recognised Accounting Practice, GRAP 19, Provisions were not identified and included in the financial statements. I was unable to determine the correct value of provisions to be separately disclosed in the current year as it was impracticable to do so.

Unspent conditional grants

39. I was unable to obtain sufficient appropriate audit evidence for the balance of unspent conditional grants disclosed as R7 009 261 (2011: R4 262 638) in note 9 to the financial statements due to the limitations communicated in paragraphs ~~xx~~ of this report.
40. I was unable to obtain sufficient appropriate audit evidence for the restatement in the corresponding figure of unspent conditional grants. As described in note 32 to the financial statements, the restatement of R385 058 was made in order to rectify a prior year misstatement. I was unable to confirm the restatement by alternative means.
41. During 2011 I was unable to audit the difference between the trial balance and the amounts disclosed in the annual financial statement to the amount of R728 186.

Consequently, I was unable to determine whether any adjustments to the unspent conditional grants corresponding figure was necessary.

Cash flow statement

42. I was unable to confirm the current and comparative cash flow statement to the financial statements is correct due to the limitations experienced as included under the basis of disclaimer paragraphs. I was not able to perform alternative procedures. Consequently, I was unable to determine whether any adjustment relating to the cash flow statement in the financial statements was necessary.

Long term liabilities

43. I was unable to confirm that the payments for long-term liabilities to the amount of R339 258 stated at R123 649 in note 2 to the financial statements regarding finance leases that was included in the amortisation tables agreed to payments received by third parties due to sufficient appropriate audit evidence not being available. I was unable to

perform alternative procedures. Consequently I was unable to determine whether any adjustment relating to long-term liabilities in the financial statements was necessary.

Intangible assets

44. A number of intangible assets were not included in the financial statements as required by Standards of Generally Recognised Accounting Practice, GRAP 31, Intangible assets, which lead to intangible assets that are disclosed as R15 492 in note 13 to the financial statements being understated and accumulated surplus being overstated. I was unable to determine the correct value of intangible assets to be separately disclosed as it was impracticable to do so.

Commitments

45. The municipality did not have adequate systems in place to identify and disclose all commitments accurately at year-end as per Standards of Generally Recognised Accounting Practice, GRAP 17, Property, plant and equipment. Alternative procedures confirmed that commitments are understated. I was unable to determine the correct value of commitments to be separately disclosed as it was impracticable to do so.

Fruitless and wasteful expenditure

46. I was unable to confirm the opening balance for fruitless and wasteful expenditure to the amount of R98 676 included in note 39 to the financial statements due to a lack of sufficient appropriate audit evidence. I was unable to perform alternative procedures. Consequently, I was unable to determine whether any adjustment relating to fruitless and wasteful expenditure in the financial statements was necessary.
47. The municipality did not include particulars of fruitless and wasteful expenditure in the notes to the financial statements as required by section 125(2)(d) of the MFMA. The municipality made payments that could have been avoided had reasonable care been exercised. I was unable to determine the correct value of fruitless and wasteful expenditure to be separately disclosed as it was impracticable to do so.

Contingent liabilities

48. I was unable to confirm contingent liabilities to the amount of R715 650 as disclosed in note 48 to the financial statements as sufficient appropriate audit evidence was not submitted. External confirmations were not provided by the third parties. I was unable to perform alternative procedures. Consequently, I was unable to determine whether any adjustment relating to contingent liabilities in the financial statements was necessary.
49. A brief description of the nature of the contingent liabilities disclosed in note 48 was not always included as per the requirement of Standards of Generally Recognised Accounting Practice, GRAP 19, Provisions, contingent liabilities and contingent assets.

Material losses

50. I was unable to confirm that sufficient appropriate audit evidence regarding the prior year material losses disclosed in note 39 to the financial statements exists. I was unable to perform alternative procedures. Consequently, I was unable to determine whether any adjustment relating to material losses in the financial statements was necessary.
51. The particulars of the material losses in the form of amounts were not disclosed in note 39 as required by section 125 (2) (d) of the MFMA. I was unable to determine the correct

value of material losses to be separately disclosed as it was impracticable to do so.

Disclaimer of opinion

52. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matters

53. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Significant uncertainties

54. With reference to note 48 to the financial statements, contingent liabilities, the municipality is the defendant in a number of law suits. The ultimate outcome of these matters cannot presently be determined.

Restatement of corresponding figures

55. As disclosed in note 32 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of errors discovered during 30 June 2012 in the financial statements of the Phokwane local municipality at, and for the year ended, 30 June 2011.

Material under spending of the budget

56. As disclosed in note 38, the municipality has materially under spent the budget on parks and recreation, water and electricity to the amount of R24 999 475 and the capital budget to the amount of R32 846 813. The draft annual report was not received within the legislated timeframes. Subsequently, it was not possible to determine the effect on service delivery of the under spending of the budget.

Additional matters

57. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Material inconsistencies in other information included in the annual report

58. The annual report had not been received at the date of this report, with the result that a conclusion could not be drawn on the consistency between the financial statements and the audit report with other information included in the annual report.

Unaudited supplementary schedules

59. The supplementary information set out on pages ~~xxx~~ to ~~xxx~~ does not form part of the financial statements and is presented as additional information. I have not audited this schedule and, accordingly, I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

60. In accordance with the PAA and the General Notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance

with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

61. The annual performance report included in the annual report was not presented in time for audit and consequently my findings below are limited to the procedures performed on the strategic planning and performance management documents.
62. The information was assessed to determine whether performance indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury *Framework for managing programme performance information*.

Usefulness of information

63. The National Treasury Framework for managing programme predetermined objectives (FMPPi) requires that it must be possible to validate the processes and systems that produce the indicator. A total of 100% of the measures relevant to Objective 2: Sanitation and Objective 5: Housing were not verifiable in that valid processes and systems that produce the information on actual performance did not exist.
64. This was due to the lack of key controls in the relevant systems of collection, collation, verification and storage of actual performance information.

Compliance with laws and regulations

65. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the General Notice issued in terms of the PAA are as follows:

Strategic planning and performance management

66. The municipality did not afford the local community at least 21 days to comment on the final draft of its integrated development plan before the plan was submitted to council for adoption, as required by regulation 15(3) of the municipal planning and performance management regulations.
67. Sufficient appropriate audit evidence was not submitted to confirm that the municipality gave effect to its integrated development plan and conducted its affairs in a manner which was consistent with its integrated development plan, as required by section 36 of the Municipal Systems Act and municipal planning and performance management regulation 6.
68. The municipality did not establish a performance management system, as required by section 38 (a) of the Municipal Systems Act.
69. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the Municipal Systems Act.
70. The municipality did not monitor performance, with regard to each of the development

priorities and objectives included in the IDP and against the key performance indicators and targets set.

71. The municipality did not measure and review performance at least once per year, with regard to each of those development priorities and objectives and against the key performance indicators and targets set.
72. The municipality did not take steps to improve performance with regard to those development priorities and objectives where performance targets were not met, as required by section 41 of the Municipal Systems Act.

Budget

73. Expenditure was incurred that was not budgeted for, in contravention of section 15 of the MFMA.
74. Sufficient appropriate audit evidence was not submitted to confirm that the initial two quarterly reports were submitted to the council on the implementation of the budget and financial state of affairs of the municipality within 30 days after the end of each quarter, as required by section 52(d) of the MFMA.
75. Revisions to the service delivery and budget implementation plan were not approved by the council after the approval of the adjustments budget, as required by section 54(1)(c) of the MFMA.
76. Certain monthly budget statements were not submitted in time to the relevant provincial treasury, as required by section 71(1) of the MFMA.
77. The accounting officer assessed the first half of the financial year performance of the municipality by 8 February 2012 and not by 25 January 2012, as required by section 72(1) and 72(1)(a)(ii) of the MFMA.

Annual financial statements, performance and annual reports

78. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors were not adequately corrected, which resulted in the financial statements receiving a disclaimer opinion.
79. The 2010-11 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.
80. A written explanation was not submitted to council setting out the reasons for the delay in the tabling of the 2010-11 annual report in the council, as required by section 127(3) of the MFMA.
81. The accounting officer did not make the 2010/11 annual report public immediately after the annual report was tabled in the council, as required by section 127(5)(a) of the MFMA.

Audit committee

82. The audit committee was appointed on 1 February 2012. The audit committee did not advise the council, the political office bearers, the accounting officer and management

staff on matters relating to internal financial control and internal audits, risk management, accounting policies, effective governance, performance management and performance evaluation throughout the year, as required by section 166(2)(a) of the MFMA.

83. The audit committee did not review the annual financial statements to provide the council with an authoritative and credible view of the financial position of the entity, its efficiency and effectiveness and its overall level of compliance with the MFMA, DoRA and other applicable legislation, as required by section 166(2)(b) of the MFMA.
84. The audit committee did not respond to the council on the issues raised in the audit reports of the Auditor-General during 2011-12, as required by section 166(2)(c) of the MFMA. This was due to the audit committee only being appointed in February 2012.
85. A performance audit committee was not in place and the audit committee established in terms of MFMA section 166(1) was not used for this function, as required by municipal planning and performance management regulation 14(2)(a).

Internal audit

86. The internal audit unit did not function as required by section 165(2) of the MFMA, in that:
 - it did not prepare a risk-based audit plan and an internal audit programme for the financial year under review.
 - it did not advise the accounting officer and/or report to the audit committee on matters relating to accounting procedures and loss control.
87. The internal audit unit did not report to the audit committee on all matters relating to compliance with the DoRA and other applicable legislation, as required by section 165(2)(b) of the MFMA.
88. The internal audit did not audit the results of performance measurements, as required by section 45(1) (a) of the Municipal Systems Act and municipal planning and performance management regulation 14(1) (a).
89. The internal audit unit did not audit the performance measurements on a continuous basis and did not submit quarterly reports on their audits to the accounting officer and the performance audit committee, as required by municipal planning and performance management regulation 14(1)(c).
90. The internal audit unit did not assess the functionality of the performance management system, whether the performance management system complied with the requirements of the Municipal Systems Act and the extent to which the performance measurements were reliable in measuring the performance of the municipality on key and general performance indicators, as required by Municipal Planning and Performance Management Regulation 14(1) (b) (i), (ii) and (iii).

Expenditure management

91. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.

92. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and accounted for payments made, as required by section 65(2)(b) of the MFMA.
93. An effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds, was not in place as required by section 65(2)(a) of the MFMA.
94. The accounting officer did not take reasonable steps to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
95. Unauthorised, irregular and fruitless and wasteful expenditure was not recovered from the liable person, as required by section 32(2) of the MFMA.

Conditional grants received

96. Sufficient appropriate audit evidence could not be obtained that the municipality evaluated its performance in respect of programmes funded by the allocation and submitted the evaluation to the transferring national officer within two months after the end of the financial year, as required by section 12(6) of the DoRA.
97. Sufficient appropriate audit evidence could not be obtained that unspent conditional grant funds were committed to identifiable projects and/or approved by the National Treasury for retention, or surrendered to National Revenue Fund, as required by section 20(1) of the DoRA.
98. Sufficient appropriate audit evidence could not be obtained that the municipality timely submitted project registration forms for projects it intended implementing in the financial year under review, to the department of local government, as required by the *Division of Revenue Grant Framework, Gazette No. 34280*.
99. Sufficient appropriate audit evidence could not be obtained that the municipality submitted project implementation plans to the national department (CoGTA), as required by the *Division of Revenue Grant Framework, Gazette No. 34280*.
100. Sufficient appropriate audit evidence could not be obtained that the municipality had registered its master plans for bulk infrastructure with the integrated national electrification programme (INEP), as required by the *Division of Revenue Grant Framework, Gazette No. 34280*.
101. Sufficient appropriate audit evidence could not be obtained that projects were implemented in line with the details contained in the integrated development plan, as required by the *Division of Revenue Grant Framework, Gazette No. 34280*.
102. Sufficient appropriate audit evidence could not be obtained that the municipality submitted its signed activity plan and/or in the prescribed format to the national department (CoGTA), as required by the *Division of Revenue Grant Framework, Gazette No. 34280*.
103. Sufficient appropriate audit evidence could not be obtained that the municipality submitted, within 20 days after the end of each month, its monthly expenditure reports to the national department (CoGTA), as required by the *Division of Revenue Grant*

Revenue

104. An adequate management, accounting and information system was not in place which recognised revenue when it was earned, accounted for debtors and accounted for receipts of revenue, as required by section 64(2)(e) of the MFMA.
105. An adequate credit control and debt collection policy was not implemented, as required by section 96(b) of the Municipal Systems Act and section 62(1)(f)(iii) of Municipal Finance Management Act.
106. The municipality contravened section 15(2) of the Electricity Regulation Act, 2006 (Act No. 4 of 2006) (ERA) by charging electricity tariffs in excess of those approved by NERSA. This contravention by the municipality may result in penalties being imposed by the Regulator in terms of section 18 of ERA.

Asset management

107. Sufficient appropriate audit evidence was not submitted to confirm that an adequate management, accounting and information system which accounts for assets was in place, as required by section 63(2)(a) of the MFMA.

Supply chain management

108. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) and (c).
109. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy in contravention of SCM regulations 16(b) and 17(b).
110. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
111. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R200 000 were procured by means of inviting competitive bids and that deviations were approved by the accounting officer only if it was impractical to invite competitive bids, as required by SCM regulations 19(a) and 36(1).
112. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as per required by SCM regulation 27(2)(a).
113. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM regulation 22(1) & 22(2).
114. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders based on points given for criteria that were stipulated in the original invitation for bidding and quotations, as required by SCM regulations 21(b) and 28(1)(a) and preferential procurement regulations.

115. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality, as required by SCM regulation 28(2).
116. Sufficient appropriate audit evidence could not be obtained that bid adjudication was always done by committees which were composed in accordance with SCM regulation 29(2).
117. The preference point system was not applied in all procurement of goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act and SCM regulation 28(1) (a).
118. Sufficient appropriate audit evidence could not be obtained that the preference point system was applied in all procurement of goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act and SCM regulation 28(1)(a).
119. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to suppliers based on preference points that were allocated and calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.
120. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders that scored the highest points in the evaluation process, as required by of section 2(1)(f) of Preferential Procurement Policy Framework Act.
121. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
122. Quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.
123. Sufficient appropriate audit evidence could not be obtained that contracts were only awarded to providers whose tax matters have been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.
124. A list of accredited prospective providers was not in place for procuring goods and services through quotations, as required by SCM regulation 14(1) (a).
125. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements and a procurement process which is fair, equitable, transparent and competitive, as procurement documentation was not submitted by management.
126. Contracts and quotations were awarded to bidders who did not submit a declaration as to whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
127. Quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.

Human resource management

128. An acting accounting officer was appointed for an additional period of three months in excess of the three month extension already granted by the MEC of local government, in contravention of section 54A(2A)(a) of the Municipal Systems Act.
129. Appointments were made in posts which were not provided for in the approved staff establishment of the municipality, in contravention of section 66(3) of the Municipal Systems Act.
130. Job descriptions were not established for all posts in which appointments were made in the current year, in contravention of section 66(1) (b) of the Municipal Systems Act.
131. Sufficient appropriate audit evidence could not be obtained that the municipality appointed an accounting officer who had been dismissed for financial misconduct after expiry of 10 years.
132. The senior managers directly accountable to the accounting officer did not sign the correct performance agreements, as required by section 57(2) (a) of the Municipal Systems Act.
133. The performance agreements of the accounting officer senior manager and head of supply chain who did not have the minimum competencies, did not include the attainment of minimum competencies as a performance target, as required by the municipal regulations on minimum competency levels 16(2).

Internal control

134. I considered internal control relevant to my audit of the financial statements, performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion, the findings on performance information and the findings on compliance with laws and regulations included in this report.

Leadership

135. The following challenges were experienced that contributed to the weaknesses in the financial environment and the ultimate audit outcome:
 - A formally documented action plan was not implemented and monitored. The internal control weaknesses that resulted in the previous amended audit opinions were not identified and corrected.
 - Personnel had not been allocated specific duties and responsibilities to facilitate the continuous monitoring of internal controls.
 - The leadership did not take appropriate action with regard to a lack of controls in the finance and supply chain management directorates, resulting in non-compliance with applicable legislation and inadequate budget control measures. This, in turn, resulted in irregular, fruitless and wasteful as well as unauthorised expenditure.
 - Material misstatements of investments, cash and bank, property, plant and equipment, investment property, expenditure, receivables from exchange transactions, revenue, commitments, material losses and irregular expenditure

identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements and remaining supporting records that could not be provided resulted in the financial statements receiving a disclaimer audit opinion. Included above in material corrections and not corrected errors.

136. Leadership did not regularly monitor management's compliance with laws, regulations and internally designed policies and procedures. This was due to inadequate time allocated to the compliance of laws and regulations. Certain non-compliance matters were also identified at management level. There is a lack of systems to ensure compliance with all legislation. As a result, significant non-compliance issues were noted.
137. Management did not document and approve internal policies and procedures to address the process of collection, recording, processing, monitoring and reporting on predetermined objectives. This was due to a lack of understanding of the processes that should be performed to prepare a complete and valid report on predetermined objectives. Consequently, performance systems, processes and procedures had not been designed and implemented.

Financial and performance management

138. The municipality did not have individuals who sufficiently understood the financial reporting framework and performance and financial management requirements with the result that the municipality engaged a consultant to assist in the compilation of the fixed asset register and financial statements.
139. The underlying accounting records of the municipality did not facilitate the preparation of the financial statements to comply with the accounting framework.
140. Manual or automated controls were not designed to ensure that the transactions had occurred, were authorised, and were completely and accurately processed. This was due to complete business processes and a complete risk assessment not being performed. Documentation supporting amounts disclosed in the financial statements was not always available due to lack of an adequate filing system.

Governance

141. The risk of material misstatement due to fraud was not considered due to a formal fraud prevention and detection unit not being established. Sufficient controls and segregation of duties to prevent or detect fraudulent data and asset misappropriation were not implemented and maintained.
142. The municipality did not respond to the assessed risks due to a risk strategy and action plan to manage identified risks that were not performed. Consequently, internal controls were not selected and developed to prevent, detect and correct material misstatements in financial reporting and reporting on predetermined objectives.
143. The financial statements were subject to material corrections resulting from the audit, which can be attributed to the lack of risk assessments, weaknesses in the design and implementation of internal control in respect of financial management and financial reporting, and weaknesses in the information systems.

144. The accounting officer did not prioritise the establishment of a fully functioning performance audit committee and therefore the functions were not established and functional during the financial year. The audit committee was appointed in February 2012. This also resulted in the committees not being able to fulfil all their responsibilities.
145. The accounting officer did not ensure that internal audit performed a risk based audit approach and that internal audit submitted quarterly reports on predetermined objectives.

Auditor-General

Cape Town

30 November 2012



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence